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IN THE

Supreme Court of the United States

SHERMAN PARK APARTMENTS, *et al.*,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF OF *AMICI CURIAE* INSTITUTE FOR RESPONSIBLE HOUSING PRESERVATION, INSTITUTE FOR REAL ESTATE MANAGEMENT, NATIONAL AFFORDABLE HOUSING MANAGEMENT ASSOCIATION, NATIONAL ASSOCIATION OF HOME BUILDERS, NATIONAL LEASED HOUSING ASSOCIATION, AND NATIONAL MULTI HOUSING COUNCIL IN SUPPORT OF PETITIONERS

CHARLES L. EDSON
Counsel of Record
HARRY J. KELLY
NIXON PEABODY LLP
Attorneys for Amici Curiae
1255 23rd Street, N.W.
Washington, D.C. 20037
(202) 973-7700

154391

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INTEREST OF THE *AMICI CURIAE*

The *Amici Curiae* — the Institute for Responsible Housing Preservation, the Institute for Real Estate Management, the National Affordable Housing Management Association, the National Association of Home Builders, the National Leased Housing Association and the National Multi Housing Council (jointly, the "Amici") — represent a diverse group of owners, managers, investors and other persons deeply involved in affordable housing programs created pursuant to Section 221(d)(3) of the National Housing Act (the "NHA"), Pub. L. No. 83-560, 68 Stat. 590, 599 (1954), as amended by Pub. L. No. 87-70, 75 Stat. 149 (1961) (the "Section 221(d)(3) Program"), and Section 236 of the NHA, Pub. L. No. 90-448, § 201(a), 82 Stat. 476, 498-99 (1968) (the "Section 236 Program") (the Section 221(d)(3) Program and the Section 236 Program are referred to jointly herein as the "Programs").[1] The specific interest of each of the Amici is as follows:

1. The *Institute for Responsible Housing Preservation* ("IRHP") was organized by owners and managers of projects that participated in the Programs, to represent their interests in legislation, and in related administrative matters before the U.S. Department of Housing and Urban Development ("HUD") addressing prepayment of the mortgages on those projects.

2. The *Institute Of Real Estate Management* ("IREM") educates real estate managers, certifies the competence and professionalism of individuals and organizations engaged in real estate management, serves as an advocate on issues

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1. Pursuant to Rule 37 of the Rules of the Court, Petitioners and Respondent have consented to the filing of this brief and their consent letters are filed herewith. Counsel for a party did not author this brief in whole or in part, and no person or entity, other than the Amici, have made a monetary contribution to the preparation or filing of this brief. One or more of the Petitioners may be a member of one or more of the Amici.

affecting the industry, and enhances and supports its members' professional competence so they can better identify and meet the needs of those who use their services. IREM was established in 1933 and has 10,000 members across the country. Like other Amici, a number of IREM members are involved in the finance, development and management of affordable housing, including the Programs.

3. The *National Affordable Housing Management Association* ("NAHMA") was established in 1989 as a national professional association representing managers of government-assisted housing. NAHMA members presently manage more than half of the nation's privately held stock under the Programs and other Federal housing programs.

4. The *National Association of Home Builders* ("NAHB") is a leading voice in America's shelter industry. NAHB was established more than 50 years ago and represents 197,000 member firms engaged in all aspects of single family and multifamily real estate development, construction and management. Hundreds of NAHB multifamily members nationwide representing thousands of units across the country have long participated in the federal mortgage insurance programs and have actively supported their continuance.

5. The *National Leased Housing Association* ("NLHA") with 600 members nationwide was founded in 1972 as the Section 23 Leased Housing Association (Section 23 was the predecessor program to Section 8). NLHA has been deeply involved in the Programs ever since. Its members consist of private owners who participate in the Programs.

6. The *National Multi Housing Council* ("NMHC"), which was founded in 1978, represents over 700 of the apartment industry's largest and most prominent firms. Like other Amici, a number of NMHC members across the country are involved in the finance, development and management of affordable housing, and many participate in the Programs.

Like each of the Petitioners here, the Amici firmly believe that a contract exists between the Federal government and each of the owners of affordable housing projects that participate in the Programs. As explained in more detail below, the government has breached a critical part of this contract which permitted owners to prepay their insured mortgages after twenty years. The Amici submit this brief to document the nature of the contractual relationship between the Federal government and each of the owners that participated in the Programs.

SUMMARY OF ARGUMENT

1. The Petitioners and the Amici firmly believe that a contract exists between HUD and owners participating in the Programs allowing the owners to prepay their insured mortgages after twenty years. The nature of that contractual commitment can only be understood by a thorough examination of the documents that created that contract and the entire mortgage insurance process, which provides essential factual context.

2. Searching for an answer to the enduring problem of providing affordable housing to lower income families, Congress has taken several approaches. The Programs are among its most successful experiments.

Although they varied in their specifics, both of the Programs attempted to alter the economics of the multifamily real estate market to encourage the development of affordable housing. The cornerstones of the Programs were Federal insurance of the project mortgages which allowed lenders to charge lower interest rates and then further subsidization of these rates, down to 1% or 3%. The resulting savings allowed owners to charge lower rents, thereby making thousands of units of new, high quality housing affordable for lower income families. The mortgage documents, endorsed by HUD, provided that owners could prepay their mortgages and thereby terminate restrictions on rents and tenant income,

on the twentieth anniversary of HUD's final endorsement of the mortgage.

3. To participate in the Programs, owners had to complete a long and complicated process, every step of which was completely designed and controlled by HUD. All of the documents were originated by HUD, and HUD oversaw all aspects of a proposed development — from the architectural design to financing and marketing matters. Indeed, since it was Federal money, not the money of the lender, that was ultimately at stake, HUD functioned essentially as the underwriter of these loans.

The decisions by Judge Robinson of the Court of Federal Claims, *Cienega Gardens v. United States*, 33 Fed. Cl. 196 (1995) and 37 Fed. Cl. 79 (1996), carefully analyzed these documents and the operation of the Programs and properly concluded that a contract existed between HUD and the owners participating in the Programs that allowed the owners to prepay those contracts after twenty years. The lower court found that Congress breached those contracts when it enacted the Emergency Low Income Housing Preservation Act of 1987, Pub. L. No. 100-242, tit. II, 101 Stat. 1877 (1988) ("ELIPHA") and the Low Income Housing Preservation and Resident Homeownership Act of 1990, Pub. L. No. 101-625, tit. VI, 104 Stat. 4249 (1990) ("LIHPRHA"), both of which effectively barred prepayment. As the lower court realized, each of the relevant documents had to be construed together to understand the true intention of the parties. So construed, there was no question that the Federal government made a solemn promise to participating owners that they could prepay after twenty years.

4. In violation of both the standard rules of contract interpretation and, more importantly, the intention of the parties demonstrated by the history of the mortgage insurance process, the Court of Appeals for the Federal Circuit concluded that no such contract existed. *Cienega Gardens v.*

United States, 162 F.3d 1123 (Fed. Cir. 1998). The central flaw of the appellate court's analysis is its disregard for the inherent interrelation between the documents pursuant to which owners received mortgage insurance. Only by turning its back to the actual history of the mortgage insurance process could the court reach such a conclusion that conflicts with the contemporaneous understanding of all of the parties and the historical context in which they acted.

5. This brief describes in detail the mortgage insurance process that the Programs employed. It demonstrates that HUD controlled the process entirely and dictated the terms of all the relevant documents. Most importantly, it shows that at all relevant times — up to and including the date of enactment of both ELIPHA and LIHPRHA — all of the parties concurred that a contract existed between the Federal government and participating owners, allowing them to prepay their mortgages after twenty years. The Court should grant the petition here in order to assure that a large group of persons, persuaded to assist in an ambitious program for housing the nation's poor, are not denied the rights that the Federal government by contract is bound to observe.

ARGUMENT

> Although plaintiffs or their assignors *did enter into contracts with HUD in 1966 and 1968* respectively, those contracts were subject to amendment by subsequent legislation as needed for the public good.

Brief of United States at 24, *Thetford Properties IV Limited Partnership v. U.S. Department of Housing and Urban Development*, 907 F.2d 445 (4th Cir. 1990) (emphasis added).[2] In its brief filed in 1990 in a separate case involving

2. Brief of Amici Curiae In Support Of Petition For Rehearing And Suggestion Of Rehearing In Banc, Appendix at iii; *Cienega Gardens v. United States*, 162 F.3d 1123 (Fed. Cir. 1998) (Nos. 97-5126,-5134). Subsequent references to documents found in the Appendix are cited as "App. [page number]."

the rights of owners under ELIPHA, the government thus candidly acknowledged what the housing community, HUD and Congress understood from the start of the Programs: HUD was a party to a contract that allowed the owners to prepay their mortgages after 20 years.

The government has since taken a 180° turn and now maintains — *only after the present dispute arose* — there never was such a contract. Fortunately, there is ample history that documents the contemporaneous understanding of the parties from the earliest days of the Programs. The brief will allow the Court to walk through, from a contemporary perspective, the negotiation process that led to the contractual arrangement between the parties. Without question, the government's position in *Thetford* accurately states the understanding of the parties throughout the life of the Programs: HUD and the owners indeed intended to enter into a contract that allowed the owners to prepay after 20 years.

I. THE HISTORY OF THE PROGRAMS DEMONSTRATES THAT HUD PROMISED TO ALLOW PREPAYMENT AFTER TWENTY YEARS

A. Applicable Rules of Contract Construction Require the Court to Examine the Facts, the Documents and the Parties' Statements to Determine Their Intent.

As the Petition makes clear (Petition at i), the first question here is whether the Federal Circuit correctly applied traditional principles of contract interpretation. This question inevitably involves the construction of contractual language to determine the parties' intent, a matter of law that is committed to the court's consideration. *Alaska American Lumber Co., Inc. v. United States*, 25 Cl. Ct. 518, 527 (1992).

In construing contracts, courts are guided by several rules of construction directly applicable here. First, as the Court of Appeals for the Federal Circuit has previously observed, "[w]hether a legally enforceable contract has been formed

by a meeting of the minds depends upon *the totality of the factual circumstances*." *Texas Instruments, Inc. v. United States*, 922 F.2d 810, 815 (Fed. Cir. 1990) (emphasis added). As the Court of Federal Claims explains, "the language of the contract must be given the meaning that would be derived from the contract by a 'reasonably intelligent person acquainted with the contemporaneous circumstances.' " *Alaskan American Lumber*, 25 Cl. Ct. at 527, *quoting Hol-Gar Mfg. Corp. v. United States*, 351 F.2d 972, 973 (Cl. Ct. 1965). These circumstances are especially important, because "[i]n resolving ambiguity in a contract it is proper to look at the past conduct of the parties." *Tibshraeny Brothers Construction, Inc. v. United States*, 6 Cl. Ct. 463, 470 (1984). As this brief will show, the "totality of circumstances" demonstrates that HUD controlled all aspects of the mortgage insurance process, drafting all the critical documents and providing critical approvals. The 20-year prepayment provision was central to this process and was understood by all participants to be part of the government's promise. *See* pp. 8-13, below.

Second, the documents that surround the government's promise must be considered as a whole and given the meaning the parties intended. When the mortgage insurance process is understood, it will become clear that the Regulatory Agreement, the commitment, and the endorsed deed of trust constitute components of a tightly integrated process. The appellate court erred in attempting to separate documents that the parties understood to be integrated and thus failed to give credence to the parties' obvious intent. *See* pp. 13-17, below.

Finally, the Court should consider the contemporaneous statements of the parties, before a dispute arose. In their own statements, made in contemporaneous regulations and in later declarations, the parties underscore that they understood the promise made by HUD to allow prepayment after twenty years. *See* pp. 17-20.

B. The History of the Mortgage Insurance Process Demonstrates the True Intent of the Parties.

The appellate court failed to examine the lengthy process that owners seeking mortgage insurance had to pursue in order to obtain HUD's endorsement. The omission was serious, because, fully understood, that process demonstrates that HUD was the central player, making all the key decisions, dictating the terms of the principal documents and enforcing the process which owners had to follow. By failing to examine this process, the appellate court ignored the "totality of the factual circumstances" that, the Federal Circuit has explained, must be understood to realize the parties' intentions. *Texas Instruments,* 922 F.2d at 815.

HUD's central role here in the HUD mortgage insurance process is graphically illustrated in *A Practical Guide To Low- and Moderate-Income Housing*, published in 1972 (the "*Guide*"), contemporaneous with the creation of most of the mortgages that are the subject of this case and other pending litigation in the Court of Federal Claims. *See* Guide at 3:1ff, App. xv, *et seq.*[3] The *Guide* is important, because it provides a contemporaneous explanation of the parties' understanding of their contractual undertakings, before a dispute concerning the 20-year prepayment provision arose. As the Federal Circuit explains, "[o]ne may not ignore the interpretation and performance of a contract . . . before a dispute arises." *Alvin Ltd. v. United States Postal Service*, 816 F.2d 1562, 1566 (Fed. Cir. 1987); *KMS Fusion, Inc. v. United States*, 36 Fed. Cl. 68, 77 (1996) (to determine parties' intent, court should examine all "relevant circumstances . . . including the conduct of the parties before the advent of the controversy. . . .").

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3. The *Guide* was written by Charles L. Edson and Bruce S. Lane, then-partners of the firm of Frosh, Lane and Edson. Mr. Edson is counsel to the Amici filing this brief.

1. The Feasibility Stage. As described in the *Guide*, HUD formulated the entire mortgage insurance process, dictating the terms of the documents and "establish[ing] a rigid timetable for each of the stages" in that process. *Guide* at 3:1, App. v. For example, HUD issued guidance on site selection and scheduled a "pre-feasibility conference" with would-be developers, to review critical information such as the site, need and market for subsidized housing. *Guide* at 3:3, App. vii. Significantly, although the pre-feasibility conference was attended by a HUD officer, the developer and, sometimes, the developer's attorney and architect, it was not attended by the lender, who only appeared formally at the later stages of the process. *Guide* at 3:4, App. viii; *see* p. 8, below.

The *Guide* explains that a critical component of the insurance application process was the development of a management plan, governed by a "management guidebook" drafted by HUD, which

> assembles all the pertinent information, forms, and checklists that relate to management of the project. Included are such items as the *model form of lease* for use under Section 236 . . . ; the *model form of lease* for use under the rent supplement program . . . ; the application for tenant eligibility for rent supplement . . . ; a *model management agreement* . . . ; and several examples of *viable management programs*. . . .

Guide at 3:5-3:6, App. ix-x (emphases added). Thus, HUD controlled the form of all critical documents, including the leases and management agreement that the owners were allowed to use in their insured projects.

Next, the owner submitted a formal Application for Project Mortgage Insurance, designated as HUD Form 2013. *Guide* at 3:6, App. x. Relying on this and other documents provided by the owner, HUD prepared its Form 2264, the

Project Income Analysis and Appraisal, which allowed HUD "to prepare its own appraisal of the proposed project and to determine its economic feasibility." *Guide* at 3:7, App. xi. Again, HUD was not merely insuring a loan, but undertaking a full underwriting of the loan, on the basis of documents and criteria that it controlled.

Assuming HUD's analysis was favorable, HUD scheduled a "feasibility conference" to review design, marketing, site and economic feasibility issues. *Guide* at 3:8, App. xii. If the conference ended successfully, HUD would issue its "Feasibility Letter," defining cost limitations, mortgage and land value and other critical information. *Guide* at 3:9, App. xiii. The *Guide* notes that the letter designated a HUD "design representative," who "must approve the design plans for the project." *Id.*, n.10. The Feasibility Letter also set target dates which, if not met, could doom a project. The *Guide* warns that "[t]arget dates . . . are meant to be kept, and failure to do so may very well mean loss of the right to proceed to a commitment." *Id.*

2. The Commitment Stage. After the Feasibility Letter was issued, the developer had to obtain architectural drawings, and select a contractor, among other steps. *Guide* at 3:9-3:11, App. xiii-xv. When these steps were complete, the developer filed another Form 2013, in preparation for obtaining a conditional mortgage insurance commitment from HUD. *Guide* at 3:12-3:13, App. xvi-xvii.

Significantly, it was usually at this stage that the owner selected a lender to finance construction. The lender might be consulted from time to time, but seldom played a significant role in negotiations. *Guide* at 3:11-3:12, App. xv-xvi. Generally, throughout the mortgage insurance process, the primary negotiators were HUD and the owner. This result should not be surprising: to the extent that there was a financial risk in the loan, that risk was carried by HUD, not the lender. This accounts for HUD's control and strict

oversight over the insurance process. This relationship — intense negotiations between HUD and the owner with the lender in a tangential role — is the exact opposite of the picture painted by the appellate court, which assumed the primary legal relationship was between the owner and the lender, with HUD in a subservient posture. Because it fundamentally misunderstood the roles of the HUD, the owner and the lender, the appellate court was unable to understand their contractual relationship and the nature of HUD's commitment to allow prepayment after 20 years.

Typically, HUD issued a conditional commitment when the developer's documentation was complete. *Guide* at 3:11-3:12, App. xv-xvi. Following the issuance of the conditional commitment, the developer arranged to have the architect prepare final plans, and finalized construction lending arrangements. *Guide* at 3:12, App. xvi. The owner next updated prior filings, submitted additional documents and requested that HUD issue a firm commitment, which is the "commitment" that the appellate court referred to. *Cienega Gardens*, 162 F.3d at 1130. When the documentation was complete, the parties scheduled the "initial closing," which, as described by the *Guide*, resembles virtually all real estate transaction closings:

> At the initial closing, *like any other real estate closing*, all necessary documents are executed and delivered and HUD places its initial endorsement on the credit instrument. . . . HUD requests that all initial closing forms be submitted for review approximately 15 days prior to the initial closing. *This allows a HUD attorney to check for any errors or omissions that could cause a delay in closing*. In addition, especially for the inexperienced developer, HUD advises that a mock closing, or pre-closing conference, be held several days before the real one. *In this way each participant learns in advance what is expected of him.*

Guide at 3:13, App. xvii (emphases added). At the initial closing, attendees included the HUD attorney, "who directs the proceedings by calling for the desired forms," a representative of the lender, a representative of the developer, the developer's attorney and contractor, and the local HUD office director, who actually endorsed the note. The *Guide* describes HUD's direct control of these proceedings:

> Upon entering the closing room, the participants sign an attendance list, which becomes part of the record of the proceedings. *Most HUD offices assign the participants seats, and they are not expected to wander about during the closing.* The HUD counsel conducts the proceedings by calling for each form . . .

Guide at 3:14, App. xviii (emphases added). Thus, HUD did not merely dictate the content of the papers. Its control went so far as to actually assigning the parties' seats and maintaining discipline.

Significantly, it was only at this time that the familiar documents that the appellate court described — the Regulatory Agreement and the deed of trust note — were presented, along with a battery of other transactional documents that "collectively . . . form the heart of the transaction." *Guide* at 3:17, App. xviii-xxi. If all papers were in order, the local HUD officer issued HUD's firm commitment and initial endorsement of the note and the initial request for mortgage advance was presented to HUD. These initial advances usually covered architect and attorneys fees, HUD's 3 percent commitment fee, and HUD's inspection fees. At that point, the project construction started, with HUD inspecting the construction's progress and the owner developing tenant selection and assignment criteria. *Guide* at 3:18-3:20, App. xxii-xxiv.

3. The Final Closing Stage. When construction was nearly complete, the parties prepared for final closing, which resulted in the final endorsement of the mortgage insurance. *Guide* at 3:20, App. xxiv. Again, the familiar closing team is assembled — "attorneys for the mortgagee, mortgagor, and HUD and officials of the mortgagee, mortgagor, contractor, title company, and HUD" — and final documents are submitted to HUD. *Guide* at 3:21, App. xxv. Finally, as the *Guide* explains,

> If these actions have been acceptably accomplished and all commitment conditions have been complied with, the note will be endorsed by an authorized HUD official. The endorsement states that "A total sum of $____ has been approved for insurance hereunder by the Commissioner," and bears the signature of the "Agent" with the date endorsed.

Guide at 3:23, App. xxvii. At this point, the development period is complete and the project's mortgage insurance in place.

Virtually ignored by the appellate court, the mortgage insurance process demonstrates that HUD was not an isolated player in the Programs, but the ringmaster, setting schedules, creating forms, determining every phase of the insurance application process, and playing the tune to which all the private participants danced.

C. The Mortgage Insurance Process Explains The Parties' Understanding of The Relation Between the Contract Documents.

Properly understood, the mortgage insurance process discloses the full intent and understanding of the parties in much richer detail than the appellate court's surgical analysis of the regulatory agreement and the deed of trust note. As this narrative shows, these documents cannot be considered as separate and divisible instruments, any more than HUD

can be removed from the process. Rather, these documents were elements in a much larger and more complex process, dictated and controlled solely by HUD.[4] Prior to the time when the present dispute arose, HUD, the owners and the other parties understood that the Regulatory Agreement, the deed of trust and the other documents were all components of the elaborate and detailed insurance process.

The appellate court's treatment of the Regulatory Agreement is a good example of its mistaken understanding of the parties' intent. In its opinion, that court concluded that the Regulatory Agreement was essentially an isolated and separate agreement between the owner and HUD, which contained no mention of prepayment. *See* 162 F.3d at 1132 ("We start from the premise that the United States . . . was a named party to only one contract . . . , that contract being the regulatory agreement"). In fact, the Regulatory Agreement was created at the time of the initial closing — approximately midway through the insurance process — and was an integral step to the overall insurance program. HUD needed to assure that the owner would agree to its program requirements, such as HUD administrative scrutiny, tenant selection criteria, rent restrictions, and so on, because at approximately the same time, HUD would insure the first draw on the construction loan. *See* pg. 12, above. Thus, the Regulatory Agreement was not, as the appellate court seemed to feel, an unrelated and idiosyncratic agreement between HUD and the owner. *Rather, it was an essential predicate to*

4. The appellate court also failed to acknowledge "the common-law rule of contract interpretation that a court should construe ambiguous language against the interest of the party that drafted it." *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 62 (1995); *Hills Materials Co. v. Rice*, 982 F.2d 514, 516-517 (Fed. Cir. 1992) (Mayer, J); *Fort Vancouver Plywood Co. v. United States*, 860 F.2d 409, 414 (Fed. Cir. 1988). There is no dispute that HUD created all of the mortgage insurance documents. It should not be allowed to escape liability here by arguing that its own documents do not create a binding contract.

the provision of mortgage insurance. HUD's final endorsement to the actual deed of trust note that carried the prepayment rider can be seen merely as a final ratification of a multi-party agreement made at the time of the initial endorsement.

The appellate court demonstrates its misunderstanding of the parties' intent when it states that "it was the Owner, not HUD, that assumed obligations under the regulatory agreement." 162 F.3d at 1132. That statement cannot on its face be true, because it would mean that the regulatory agreement was void because it lacked mutual obligation. "A promise is illusory when it creates no obligation whatsoever on the part of the purported promisor." *Spacek v. Maritime Assn.*, 134 F.3d 283, 297 (5th Cir. 1998), citing Restatement (Second) of Contracts § 2, Comment e (1981). Of course, the consideration that supports the Regulatory Agreement is the provision of subsidies and mortgage insurance by HUD. If anything, the apparent lack of mutuality underscores the conclusion that the Regulatory Agreement must be read in conjunction with the loan documents that HUD endorsed, demonstrating that it was a party to the prepayment promise in the deed of trust rider.

The panel's mistaken separation of the Regulatory Agreement and the deed of trust note creates other irresolvable inconsistencies. The Regulatory Agreement clearly imposes a number of duties upon the owner, including tenant and rent restrictions. However, those restrictions only applied while the note was outstanding. HUD, the owner and the other parties all knew that the owner's obligations under the Regulatory Agreement hinged on the existence of the insured mortgage. Thus, the prepayment provision was a critical term, not just to the relation between the lender and the owner, but to the overall relation between HUD and the owner. ***The Regulatory Agreement and the note were not two separate documents but instead together established the nature and the length of the owners' obligations to HUD.***

The mortgage insurance process also demonstrates the critical importance of the firm commitment issued by HUD, a document that the appellate court glossed over. As the narrative shows, the commitment was a crucial document, because it permitted the parties to go to the initial closing, which in turn allowed the lender to make initial advances without which construction could not commence. *See* pp. 10-12, above. As its name implies, the commitment was just that — a promise to insure the mortgage, so long as subsequent conditions were met. Significantly, in making these promises, HUD offered its insurance under "the Regulations . . . now in effect." *See* Commitment For Insurance of Advances, App. xxviii. But, as Judge Archer's dissent correctly pointed out, *HUD's then-existing regulations expressly allowed for prepayment of the owners' mortgages after 20 years.* 162 F.3d at 1139; 24 C.F.R. § 221.524(a)(ii) and 236.30(a)(i)(1970). Thus, in offering to extend mortgage insurance subject to conditions subsequent, HUD thus bound itself to abide by the 20-year prepayment provision.[5] At the very least, the commitment demonstrates that all the parties at the time understood that the owners enjoyed a 20-year prepayment right, reflected both in HUD's own regulations and ultimately, the deed of trust note signed by the parties and endorsed by HUD.

Indeed, it is hard to imagine how the parties could evidence their mutual agreement to the prepayment provision any more clearly. It would be inappropriate, in light of this structure, for HUD and the owner to include a prepayment provision in the Regulatory Agreement, for example, since that document presumably was not intended to alter the

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5. The only alternative view — that HUD merely bound itself to observe the 20 year prepayment rule for so long as it chose to abide it — exemplifies "an absolutely classic description of an illusory promise," according to Justice Scalia. *United States v. Winstar Corp.*, 518 U.S. 839, 921 (1996) (Scalia, J., concurring in the judgment).

lenders' rights. Likewise, it would not be expected that HUD would be a full signatory to the deed of trust note, since it was not obliged to pay the lender except in the event of the owner's default. Instead, it endorsed the note, signifying, as the narrative shows, the successful completion of the mortgage insurance process and, more importantly, its agreement to provide its insurance *pursuant to the terms of the deed of trust note, the form of which it dictated.* In looking for a three-way agreement, expressly stating HUD's consent to the prepayment provision, the appellate court sought something that the parties knew was unnecessary and, as a matter of documentation, fully established elsewhere.

D. The Parties' Own Statements Underscore HUD's Consent to the Prepayment Provision.

As noted above, the parties' own conduct, prior to the eruption of a dispute, is strong evidence of the nature of their contractual intent. *Alvin Ltd.*, 816 F.2d at 1566. The fact that the parties made few contemporaneous references to the prepayment provision is itself indication that the parties understood and abided by the rights provided in the deed of trust note's rider. Nevertheless, the record shows that there is no dispute that at all relevant times, the parties recognized that right.

First, and most obviously, HUD's own regulations were an apparently unmistakable signal that HUD not only agreed to the prepayment provision, but required that all loans subject to its mortgage insurance carry the required prepayment language. *See* pg. 16, above. There can be few better examples of the parties' intent that these express regulations, the terms of which were swept into the parties' agreement by the commitment and the subsequent endorsement.

In fact, as Judge Archer points out, HUD has never rebutted the Petitioners' claim that the parties understood that HUD contracted to abide by the prepayment provision.

See 162 F.3d at 1137. If the appellate court is correct in its conclusion that there is no factual dispute (162 F.3d at 1130), one fact that clearly is not disputed is the parties' contemporaneous understanding of the prepayment provision.

Even later, however, when the first issues arose about prepayment, HUD did not actually challenge the existence of a contractual right to prepay:

> *It is our position that there was a contractual relationship between the Federal Government and private owners*, that was negotiated at that time, and at this point in time there is an arm's length transaction that cannot be changed.

Loss of Subsidized Multifamily Housing Units: Hearings Before the Subcomm. on Housing and Community Development of the House Comm. on Banking, Finance and Urban Affairs, 99th Cong., 2d Sess. 17 (1986) (testimony of R. Hunter Cushing, Deputy Assistant Secretary for HUD's Multifamily Housing Programs) (emphasis added). As Mr. Cushing admitted, the prepayment provision was intended "to get [the developers] involved in the program . . . to try and convince them to get in the program." *Id.* at 18. In light of Mr. Cushing's unambiguous declaration in 1986 that a contract existed, it shocks the conscience that the government now argues that a contract did not exist.

The Conference Report on LIHPRHA also reported that "the House Amendment established a mechanism *for recognizing the property owners' contractual interest* while not paying overly generous benefits to owners." H.R. Rep. 101-943, 101st Cong. 2d Sess. (1990) at 459 (emphasis added). Addressing then-pending legislation, two senators reflected the same understanding of the owners' contractual interest. As Senator William L. Armstrong (R. Colo.) explained, "[w]hen you curtail that [contract right], particularly when it is a contract right with a sovereign, it

might well be that some court, a circuit court or the Supreme Court might find that to be unconstitutional." 136 Cong. Rec. S14090 (daily ed. Sept. 27, 1990) (statement of Sen. Armstrong). Similarly, Senator Howell Heflin (D-Ala.) warned that "the very notion of unilaterally abrogating a contract, which has been adhered to by one party for 20 years, flies in the face of the law." 136 Cong. Rec. S14091 (daily ed. Sept. 27, 1990) (statement of Sen. Heflin).[6]

While the Amici agree that these statements cannot themselves create a contractual relationship if it did not exist earlier, *they clearly demonstrate that as late as 1990, the Federal government itself admitted that a contract existed between the owners and HUD allowing them to prepay their mortgages after 20 years*. Certainly, Secretary Kemp would not have made his statements (*see* n. 6) unless he believed that there was a true contractual arrangement, and Congress would not have committed over a billion dollars of the national fisc to compensate owners for contract violations if they believed that the parties never had a contract in the first place.

Indeed, even in later litigation involving ELIHPA, HUD admitted that a contract to allow for prepayment after 20 years existed between HUD and the owners. *Thetford Properties IV Limited Partnership v. Department of Housing and Urban Development*, 907 F.2d 445 (4th Cir. 1990). In

6. The appellate court dismissed portions of the legislative history of the prepayment legislation, ELIHPA and LIHPRHA, as "after-the-fact" declarations which cannot create a contractual relationship. 162 F.3d at 1134. In fact, the statements made at the time that the legislation was enacted are extraordinarily important. For example, Jack Kemp, then-Secretary of HUD, explained the need to "come up with a . . . proposal that would solve [the prepayment] problem without either continuing the moratorium or *having us violate the terms of the contract*." *HUD Legislative Proposals: Hearing Before the Subcomm. on Housing and Community Development of the House Comm. on Banking, Finance and Urban Affairs*, 101st Cong., 2d Sess. 42 (1990) (emphasis added).

that case — which focused on issues of exhaustion of administrative remedies — HUD conceded that the plaintiff-owners, *"did enter into contracts with HUD in 1966 and 1968"* in connection with their Section 221(d)(3) mortgages. Brief of United States at 24 (App. iii) (emphasis added). Thus, as late as 1990, HUD would not deny the obvious and dispute that the owners had a contractual right to prepay.[7]

After inducing the owners to enter into these contracts with a promise to prepay after 20 years, and maintaining that position steadfastly through that 20 year period until the very eve of the filing of the present litigation, the government should not ask this Court to sanction its unprincipled change of position.

CONCLUSION

By concentrating improperly on individual documents and ignoring the intent of the parties evidenced by the "totality of circumstances" surrounding the mortgage insurance process, the appellate court reached a conclusion that would have startled anyone attending a final closing of an insured loan and that was adopted by the government only when the case began. To prevent an enormous injustice, the Court should grant the Petition.

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7. The appellate court here disposes of the statement in *Thetford* that the Regulatory Agreement created the contractual right for the owners to prepay as mere dictum. 162 F.3d at 1132. We now know, however, that the Fourth Circuit based its opinion on the government's brief, acknowledging that a contract in fact did exist.

Respectfully submitted,

CHARLES L. EDSON
Counsel of Record
HARRY J. KELLY
NIXON PEABODY LLP
Attorneys for Amici Curiae
1255 23rd Street, N.W.
Washington, D.C. 20037
(202) 973-7700